In the United States Bankruptcy Court
for the
Southern District of Georgia
Savannah Division

In the matter of:

JAMES A. FOGARTY
GEORGIA A. FOGARTY

Debtors

BENJAMIN S. EICHHOLZ,
as Agent

Movant

vs.

JAMES A. FOGARTY
GEORGIA A. FOGARTY

Respondents

Chapter 13 Case

Number 91-40237

FILED
at 9 O'clock & 08 min AM
Date 12/18/91
MARY C. BRETON, CLERK
United States Bankruptcy Court
Savannah, Georgia

MEMORANDUM AND ORDER

The above-captioned Motion for Relief from Stay filed by Benjamin

S. Eichholz, as Agent, ("Movant") came on for hearing before this Court on September 6, 1991. Also scheduled for hearing at that time was the Motion to Avoid Lien filed by the Debtors. At the conclusion of the hearing the record was left open for a period of three weeks to allow the parties to submit additional evidence on the question of value and to file briefs in support of their respective positions. Having considered the evidence adduced at the hearing, the additional evidence and briefs submitted by the parties and applicable legal authority, this Court makes the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

James A. Fogarty and Georgia A. Fogarty ("Debtors") entered into a loan transaction agreement on or about November 17, 1989, to finance the equity portion of the purchase price of certain real property located at 5506 Waters Drive ("Waters Drive Property").

The subject loan was brokered through The Sheftall Company, a sole proprietorship wholly owned by Benjamin S. Eichholz with the actual loan proceeds in the amount of $68,000.00 being advanced by the then-undisclosed principal, Arnold J. Moss ("Moss").

Testimony adduced at the hearing and documents admitted in evidence revealed the mechanics of the loan transaction to be as follows: On November 17, 1989, the Debtors executed a Promissory Note ("Note") in the principal sum of $68,000.00, plus interest accruing thereon at the rate of twenty percent (20%) per annum. The Note was a balloon note made payable to Movant with a single payment in the amount of $81,600.00 coming due thereunder on November 17, 1990. The Note was secured by three separate parcels of real estate described in a Deed to Secure Debt ("Security Deed") executed by both Debtors in favor of Movant on November 17, 1989. The three separate parcels are the Waters Drive Property, 2330 Toussaint Avenue ("Toussaint Property"), and 77 Timberline Drive ("Timberline Property") (hereinafter sometimes referred to collectively as the "Subject Property"). The $81,600.00 balloon payment was comprised of the following components: $58,000.00

principal and $13,600.00 interest accrued over a period of twelve (12) months at the rate of 20% per annum. Of the $68,000.00 principal portion advanced by Moss to fund the loan transaction, $15,000.00 was paid as an origination fee, $3,000.00 was paid in attorney's fees, and $50,000.00 was disbursed to the control of the Debtors on November 17, 1989.

Testimony adduced at the hearing revealed that $7,500.00 of the $15,000.00 origination fee was paid to The Sheftall Company with the balance of the $7,500.00 being paid to Moss. The $3,000.00 attorney's fee was paid to Eichholz & Associates, P.C. Moss testified that he never shared in the $3,000.00 payment, never knew that such a fee was being charged and never authorized or directed that such fee be collected.

The Security Deed conveyed to Movant a second lien on the Waters Drive Property subject to a first lien which was retained by Winifred S. Shearouse, the seller of the Waters Drive Property. The Security Deed also conveyed to Movant a first lien on the Toussaint Property and a second lien on the Timberline Property,

subject to an existing first lien in favor of C&S Real Services, Inc. The balance of principal and accrued interest owed on the Subject Property as of September 6, 1991, are as follows:

(a) Movant	$ 84,946.67	(Principal plus accrued interest through 2/4/91)
	$ 13,234.25	(Additional interest accrued through 9/6/91)
	$ 98,180.92	
(b) Winifred S. Shearouse	$ 56,595.47	(Plus an indeterminate amount of additional interest accrued through 9/6/91)
(c) C&S Real Estate Services, Inc. Approximate	$ 20,000.00	(Plus an indeterminate amount of additional interest accrued through 9/6/91)
	$174,776.39	

Evidence on the issue of value of the Subject Property included the testimony of James A. Fogarty placing the value of the Waters Drive Property at around $140,000.00, the fact that the purchase price the Debtors agreed to pay for the Waters Drive Property on November 17, 1989, was $107,000.00, and the 1990 tax assessments showing a value of $97,450.00 for the Waters Drive Property, $38,050.00 for the Toussaint Property, and $42,480.00 for the Timberline Property. In view of the fact that the arm's length sale of the Waters Drive Property was approximately 10% higher than the current Chatham County tax appraisal, I conclude that the county tax figures for the Toussaint and Timberline Properties should likewise be adjusted upward by approximately 10% or $4,000.00 each. Accordingly, I conclude that the value of the three parcels of property are as follows:

Waters Drive Property	$107,000.00
Toussaint Property	$ 42,000.00
Timberline Property	$ 46,500.00
Total	$195,500.00

A Loan Commitment Letter dated November 17, 1989, from The

Sheftall Company to the Debtors which was produced at the hearing, set forth the general terms and conditions of the subject loan transaction. In particular, the letter disclosed a loan amount of $68,000.00, an interest rate of 20% per annum, a $15,000.00 origination fee, and a $3,000.00 legal fee. Each page of the letter was initialed by each Debtor. In addition, the acknowledgement portion of the letter bore the signatures of each Debtor. Each Debtor testified they received a copy of this letter on November 17, 1989.

An additional letter, dated November 17, 1989, from The Sheftall Company to the Debtors was produced at the hearing. This letter essentially confirmed the above-mentioned provisions with regard to the payment of the $15,000.00 origination fee and a $3,000.00 legal fee and also contained the acknowledgement of the Debtors. Each Debtor testified they received a copy of this letter on November 17, 1989.

A Disclosure Statement prepared in connection with the loan transaction was produced at the hearing setting forth the material terms of the

transaction, including the payment of $3,000.00 in attorney's fees, the $15,000.00 origination fee, and $13,600.00 in interest for an effective annual percentage rate of 58.83%. The statement also disclosed that the Note was payable in full on November 17, 1990, in the amount of $81,600.00. The Disclosure Statement bears the signatures of each Debtor. Each Debtor testified they received a copy of the Disclosure Statement at the loan closing.

A Notice of Right to Cancel was produced at the hearing advising the Debtors of their right to cancel the loan transaction in accordance with federal law. The acknowledgement at the bottom of this Notice states that each of the undersigned acknowledged receipt of two copies of same. The acknowledgement bore the signature of each Debtor.

A letter dated November 17, 1989, from Edward M. Buttimer, Esq., to Benjamin S. Eichholz was also produced at the hearing. This letter stated that Mr. Buttimer was closing the Debtors' purchase of the Waters Drive Property. The letter further stated that Mr. Buttimer carefully explained to the Debtors their right to

rescind the loan transaction and that they wished to waive their right to rescind based on personal hardship that waiting for the right to expire would impose on them. The letter further stated that it was Mr. Buttimer's opinion that the waiver was knowingly and intelligently made by the Debtors. Mr. Buttimer also offered testimony at the hearing to the same effect.

The Debtors failed to make any payment due under the Note, and the obligations thereunder matured in full on November 17, 1990, prior to the commencement of the Debtors' case on February 4, 1991.

As of the date of the hearing on this matter, the Debtors admitted that they have never made any payment of the principal or interest under the terms of the Note. Debtors testified that they are currently residing in the Waters Drive Property and manifested intent at the hearing to surrender the Waters Drive Property and the Timberline Property to Movant.

CONCLUSIONS OF LAW

The Motion for Relief from Stay is brought pursuant to 11 U.S.C. Section 362, alleging that Movant's interest in the Subject Property is not adequately protected and in the alternative, that there is no equity in the Subject Property and it is not necessary to an effective reorganization. The Debtors' Motion to Avoid Lien seeks to vacate Movant's interest in the Subject Property, alleging that the subject loan transaction was illegal, entered into under duress, was entered into under misleading circumstances and that it was not a secured transaction under Georgia law.

As a preliminary note, the Debtors' Motion is essentially an attempt to determine the extent and validity of Movant's interest in the Subject Property. As such, the allegations contained therein would more properly be heard in the context of an adversary proceeding. See Bankruptcy Rule 7001. The parties, however, have consented to this Court's determination of these allegations as affirmative defenses to Movant's Motion for Relief.

11 U.S.C. Section 362(d) provides:

> (d) on request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying or conditioning such stay--
>
> (1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or
>
> (2) with respect to a stay of an act against property under subsection (a) of this section, if--
>
> (A) the debtor does not have an equity in such property, and
>
> (B) such property is not necessary to an effective reorganization.

11 U.S.C. Section 362(g) provides that the Movant has the burden of proving lack of equity and the Debtor has the burden on all other issues.

A. Usury

As a first defense to the Motion for Relief, Debtors assert that the

loan transaction is usurious under Georgia law. The parties have agreed and Georgia law currently holds that a usurious loan is not void but only that the interest charged thereon would be uncollectible. *See* Norris v. Sigler Daisy Corp., 260 Ga. 271, 392 S.E.2d 242 (1990). "'Usury' means reserving and taking or contracting to reserve and take, either directly or indirectly, a greater sum for the use of money than the lawful interest." O.C.G.A. §7-4-1. Two apparently conflicting Georgia statutes attempt to define the legal rate of interest. The civil usury statute essentially states that in certain loan transactions (including the loan transaction at issue here), the parties may contract for any amount of interest:

> . . . parties may establish by written contract any rate of interest, expressed in simple interest terms as of the date of the evidence of the indebtedness . . . where the principal amount involved is more than $3,000.00 but less than $250,000.00 . . .

O.C.G.A. §7-4-2(a)(1)(A). The criminal usury statute, however, provides as follows:

> Any person, company or corporation who shall reserve, charge or take for any loan or advance of money, or

> forbearance to enforce the collection of any sum of money, any rate of interest greater than 5 percent per month, either directly or indirectly, by way of commission for advances, discount, exchange, or the purchase of salary or wages; by notarial or other fees; or by any contract, contrivance, or device whatsoever shall be guilty of a misdemeanor.

O.C.G.A. §7-4-18(a). The Georgia Supreme Court has recently addressed the apparent dichotomy between Georgia's civil and criminal usury and ruled that the provisions of the criminal usury statute apply in a civil action. Norris, 260 Ga. at 271. Therefore, the five percent interest rate cap of O.C.G.A. Section 7-4-18 would apply in the instant case to limit the legal rate of interest to 5 percent per month. In Norris, the Court also ruled that origination fees were to be considered interest for purposes of O.C.G.A. Section 7-4-18, and then went on to perform the mathematical calculations necessary to determine the effective monthly interest rate of the loan at issue therein. Using the calculations methods set out in Norris, the interest rate of the loan in the case at bar come to 4.49% if the $3,000.00 in attorney's fees are not characterized as interest for purposes of the calculation. If attorney's fees are included as interest the effective monthly interest rate comes to 5.26%. The question,

therefore, becomes whether the attorney's fees collected in the subject transaction constitute interest under Georgia law. The well established rule appears to be that attorney's fees collected as part of a loan transaction do not constitute interest. Gannon v. Scottish American Mortgage Co., 106 Ga. 510 (1898). This is particularly true where Moss neither authorized, directed nor shared in the fees paid to the attorney closing the loan transaction. Id. Even though the fees charged here are substantial, it is clear that the attorney's fees are not to be considered interest and therefore the monthly interest rate in the subject loan transaction falls within the limits set by O.C.G.A. Section 7-4-18. Therefore, I conclude that the interest portion of the subject loan transaction is a valid and enforceable obligation under Georgia law. Although the total cost of credit charged to Debtors is shocking when viewed in the abstract, it does not appear to have exceeded the maximum permissible under state law and Debtors were clearly in desperate need of a large loan on short notice which understandably exposed them to only the costliest of credit sources.

B. Truth-in-Lending Act

Debtors assert that the loan transaction was consummated in violation

of the Truth-in-Lending Act ("TILA"). 15 U.S.C. §1601, et. seq. Specifically, the Debtors assert that the waiver of their right to rescind was invalid and that this defect renders the loan transaction void.

Congress enacted TILA to ensure meaningful disclosures in consumer credit transactions. 15 U.S.C. §1601(a). It appears clear that the Debtors received all "material disclosures" about the loan transaction and notice of their right to rescind same in accordance with TILA. The Loan Commitment Letter, the Loan Confirmation Letter, the Disclosure Statement and the Notice of the Right to Rescind produced at the hearing, all bearing the signatures of the Debtors acknowledging receipt thereof, appear to set forth all material terms of the loan transaction. *See* 15 U.S.C. §1635(c). The only question is whether the waiver of the right to rescind in this case was a valid waiver and, if not, whether this defect is fatal to the loan transaction.

A consumer may exercise the right to rescind until midnight of the third business day following consummation, delivery of the notice required by 12

C.F.R. Section 226.23(b) or delivery of all material disclosures, whichever occurs last. 12 C.F.R. §226.23(a)(3).

Unless a consumer waives the right of rescission under 12 C.F.R. Section 226.23(e), no money shall be disbursed other than in escrow, no services shall be performed and no materials delivered until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded. 12 C.F.R. §226.23(c). To waive the right, the consumer shall give the creditor a dated, written statement that describes the emergency, specifically waives the right to rescind, and bears all the signatures of the consumers entitled to rescind. 12 C.F.R. §226.23(e).

While the waiver in this case would appear to have been knowingly and intelligently made, as a technical matter it does not appear to have complied with the applicable regulation since it did not bear the signatures of the consumers, but was, instead, signed by their attorney. Therefore, the funds in this case were, as a technical matter, disbursed before the expiration of the three day period for rescission, in violation of 12 C.F.R. Section 226.23(c). In any event, this finding does little to effect

the validity of the loan transaction involved, where the material disclosure requirements and notice of rescission requirements have been complied with. Smith v. Fidelity Consumer Discount Co., 898 F.2d 896 (3rd Cir. 1990); Hunter v. Richmond Equity, No. CV85-P-2734-S, Slip Op. at 9 (N.D.Ala. Nov. 23, 1987). The effect of an invalid waiver simply is that the borrowers retained their right to rescind for the full three day period, which they never exercised. Id. Such premature disbursement affords the borrowers no other rescissory relief. Id.

C. 11 U.S.C. Section 362(d)

Movant seeks relief from all stays entered pursuant to 11 U.S.C. Section 362 on the alternative grounds that his interest in the subject property is not adequately protected or that the Debtors have no equity in the property and that such property is not necessary to an effective reorganization. Because I conclude that relief is warranted on the former ground as set forth below, I make no conclusions as to the latter ground for relief.

The testimony adduced at the hearing revealed the subject loan

matured by its own terms on November 17, 1990. The burden is on the Debtors in this instance to show that Movant is adequately protected. 11 U.S.C. §362(g)(2). The Debtors admitted they have never made any payment of principal or interest on this loan. At the same time, interest both on Movant's loan and on the other two mortgages continue to accrue at their respective rates. The only evidence produced at the hearing tending to show that Movant's interest in the property is adequately protected is that relating to the existence of an equity cushion. I have concluded that the total value of these parcels is $195,500.00. The total amount of all liens on the Subject Property on the date of the hearing of this matter totalled $174,776.39, not taking into account the accrual of interest on the first mortgage securing the Waters Drive Property and the first mortgage securing the Timberline Property. This amounts to approximately a 12% equity cushion, taking all three parcels into consideration. However, given the accrual of interest on three mortgage loans, the lack of any interest or principal payments by the Debtors on Movant's loan and the absence of any evidence as to Debtors' future ability to make adequate protection payments, I find this equity cushion to be insufficient to adequately protect Movant's interest in all three of the parcels. In re Rice, 82 B.R. 623 (Bankr. S.D.Ga. 1987); In re

Kertennis, 40 B.R. 895 (Bankr. D.R.I. 1984); In re Kost, 102 B.R. 829 (D.Wyo. 1989).

However, to permit foreclosure of all three tracts would deprive Debtors of any opportunity to preserve their equity. Accordingly, I conclude that Movant is entitled to proceed to foreclose two of the three tracts, but that Debtors should be permitted to retain, for the present, one tract.

At the close of the most recent hearing I advised both parties that I would lift the automatic stay as to two of the three parcels and would consider the preferences of all parties in determining which property to permit Debtors to retain. Debtors have expressed a preference to retain the Toussaint Avenue Property, apparently because it has sentimental value to them and would be more desirable for them to occupy as a residence. Movant expresses his preference that he be permitted to foreclose on the Waters Drive and Toussaint Avenue Properties for the reason that the Toussaint Avenue Property is encumbered only by the Movant's debt deed and the Timberline Property is subject to a pre-existing first mortgage (as is the Waters Drive Property). To be specific the Timberline Property is subject to a first mortgage in

favor of C&S Real Estate Services of approximately $20,000.00, the exact balance never having been established by evidence. As a result Movant's disposition of the Waters Drive and Timberline Tracts is much less likely to result in payment in full of the obligation owed to the Movant than would foreclosure on the Waters Drive and Toussaint Avenue Properties.

Indeed, I advised Movant's counsel that if his client would accept the Waters Drive and Toussaint Avenue Properties in full satisfaction of his claim I would conclude that it was in the Debtors' best interest to have those properties surrendered. Movant's counsel subsequently advised the Court that his client did not believe it to be in his best interest to agree to the surrender in full satisfaction. On the other hand, Debtors' election to retain the Toussaint Avenue Property, if permitted, would leave Debtors owing a $25,000.00 balance to the Movant if the values determined in this Order are subsequently found to be accurate. That $25,000.00 balance would be increased by whatever expenses of sale and additional interest accrual might be added as an allowable charge to the principal and interest already accrued. That net indebtedness, as previously indicated, became immediately due and payable on

November 17, 1990. No payment of principal or any interest was made at any time after November, 1990, either before or after the filing of this case.

Under the provisions of 11 U.S.C. Section 1322(b)(2) the Debtors may modify the rights of holders of secured claims other than those claims secured only "by a security interest in real property that is the debtor's principal residence." Even though the note matured by its terms prior to the filing of the case, since the note was secured by three parcels of property only one of which could serve as the Debtors' principal residence I find that the maturity date for the balance of the obligation may be modified and Movant may not insist on an immediate right to foreclose.

Accordingly, in consideration of the Debtors' right to seek a fresh start under Title 11 and their expressed preference to retain the Toussaint Avenue Property I hereby lift the automatic stay of 11 U.S.C. Section 362 with respect to the Waters Drive and Timberline Drive Properties. The automatic stay remains in full force and effect as to the Toussaint Avenue Property. In addition, in order to avoid undue further delays in administration of this case I will estimate pursuant to 11 U.S.C.

Section 502(c) the unliquidated claim of the Movant to be $30,000.00. This amount is, of course, subject to adjustment after Movant realizes on the collateral foreclosed upon and sold, and the price at which such disposition occurs is subject to review of any court of competent jurisdiction. However, in order that the administration of this case not be delayed any further said claim is estimated until further Order of this Court at $30,000.00 which shall be treated as a fully secured claim. Debtors are ORDERED, within ten (10) days of the date of this Order, to file an amended plan detailing the manner in which said claim as now established or hereafter amended will be liquidated over the five year life of the plan or such lesser period of time as Debtors may propose.

The automatic stay of 11 U.S.C. Section 362 remains in full force and effect as to the Toussaint Avenue Property until further Order of this Court. Movant's lien and power of sale granted under the deed to secure debt and other documents executed by the Debtors cannot be exercised unless and until there is a subsequent Order of this Court lifting the automatic stay. Accordingly, Movant's right to subsequently exercise his power of sale is expressly reserved and shall not be

deemed extinguished by his prior exercise of a right of his power of sale in and to the other parcels, that is the Waters Avenue and Timberline Drive Properties.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia
This 16th day of December, 1991.